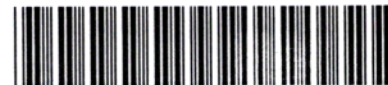


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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

DOUG LITTLE, Chairman
BOB STUMP
BOB BURNS
ANDY TOBIN
TOM FORESE

IN THE MATTER OF THE
APPLICATION OF ARIZONA PUBLIC
SERVICE COMPANY FOR A
HEARING TO DETERMINE THE FAIR
VALUE OF THE UTILITY PROPERTY
OF THE COMPANY FOR
RATEMAKING PURPOSES, TO FIX A
JUST AND REASONABLE RATE OF
RETURN THEREON, TO APPROVE
RATE SCHEDULES DESIGNED TO
DEVELOP SUCH RETURN IN THE
MATTER OF FUEL AND PURCHASED
POWER PROCUREMENT AUDITS
FOR ARIZONA PUBLIC SERVICE

Docket No. E-01345A-16-0036

Docket No. E-01345A-16-0123

**ELECTRICAL DISTRICT NUMBER
EIGHT AND MCMULLEN VALLEY
WATER CONSERVATION &
DRAINAGE DISTRICT'S
RESPONSE TO
CORRESPONDENCE FROM
COMMISSIONER BURNS
REGARDING THE SETTLEMENT
AGREEMENT**

Electrical District Number Eight and McMullen Valley Water Conservation &
Drainage District ("ED8/McMullen") hereby submit the following response to the
correspondence from Commissioner Robert L. Burns, docketed April 11, 2017,

1 regarding the proposed Settlement Agreement. ED8/McMullen offers responses to the
2 following questions which are applicable to the Direct Testimony previously filed by
3 ED8/McMullen witness, James D. Downing:

4 **Q. APS's application requested a net base rate increase of \$165.9 million.**
5 **The Settlement Agreement results in a net base rate increase of \$94.624 million**
6 **(paragraph 3.1).**

- 7 • **Why did APS agree to a net base rate increase of over \$71 million less than**
8 **requested in its application?**
- 9 • **Does APS believe that \$71 million is an insignificant amount?**
- 10 • **Does APS believe that its rate application request for a \$165.9 million net**
11 **base rate increase was inflated?**

12 **A.** Of course APS is never going to admit that its application request was
13 inflated. Rather, APS will argue that settlements are a process of "give and take," and
14 that reasonable concessions were made to reach a compromise that is "in the public's
15 best interest". But what "concessions" did APS actually make? How can APS concede
16 something it didn't have in the first place? To start from an "ask" of over \$165 million
17 and then pretend to concede something to reach a settlement is an outright illusion. As
18 soon as APS initiates settlement discussions, which is always immediately after the
19 filing of direct testimony by intervenors, the entire focus shifts away from what ought to
20 be the true baseline starting point for negotiations—zero, no rate increase, or worse, a
21 rate decrease as both Staff and RUCO's experts recommended. Instead, everyone's new
22 focal point is the inflated request that APS filed in its Application, and the new,
23 seemingly generous compromise that APS is offering to "give" out of the gate, to which
24 the intervenors predictably respond by offering their own "gives" for APS to "take".
25 From that point on, APS has completely changed the playing field to its advantage and
26 is in total control of the process.

1
2 **Q. RUCO's direct testimony recommended a net base rate decrease of**
3 **\$24.6 million. The Settlement Agreement results in a net base rate increase of**
4 **\$94.624 million (paragraph 3.1).**

- 5 • **Why did RUCO agree to a net base rate increase of over \$119 million**
6 **greater than recommended in its direct testimony?**
7 • **Does RUCO believe that its net base rate decrease recommendation**
8 **contained in its direct testimony was flawed?**

9 **Settlement Agreements are a result of give and take (see paragraph 40.1).**

- 10 • **What did RUCO receive in this Settlement Agreement for agreeing to a net**
11 **base rate increase that is \$119.2 million greater than it recommended in its**
12 **direct testimony that RUCO would not have received without this Settlement**
13 **Agreement?**

14 **A. This same line of questioning is asked of both RUCO and Staff, with the**
15 **numbers changed to reflect the slightly different numeric conclusions reached by their**
16 **respective experts. Both agencies filed testimony supporting the same underlying**
17 **premise—that APS did not need a rate increase, but instead should actually get a rate**
18 **decrease. Yet, as discussed in the Direct Testimony of James D. Downing in**
19 **Opposition to the Settlement Agreement, as soon as APS rounds up the parties to begin**
20 **settlement discussions and presents its new “compromise” offer, RUCO and Staff**
21 **immediately begin negotiating against themselves. Contrary recommendations of expert**
22 **witnesses are abandoned without explanation, deals are struck (during meetings in**
23 **which only select parties are allowed to be present), and APS avoids ever having to**
24 **actually prove anything at all.**

25 **What consideration do RUCO and Staff receive from APS in exchange for**
26 **backing off of the “no increase” positions taken by their experts? Both agencies largely**

1 justify the Settlement Agreement by arguing that it gives APS less than what it asked for
2 in its Application, or what the company *could* have received, had the case been fully
3 litigated. Merely chipping away at APS's illusory ask and avoiding protracted litigation,
4 however, is not a satisfactory answer for agencies that are charged with protecting
5 customers from the self-serving designs of an unchecked monopoly.

6 **Q. Please explain in detail how the Commission not approving this**
7 **Settlement Agreement but instead having this case be fully litigated may be**
8 **beneficial for each of the customer classes listed below:**

9 **A.** This question, posed to APS, RUCO, Staff, and EFCA, gets at the very
10 crux of the Direct Testimony of James D. Downing in Opposition to the Settlement
11 Agreement. APS continues to expand its rate base through ever increasing plant, when
12 APS's own statistical reports show that demand on APS's system has actually
13 decreased. Meanwhile APS is making record profits for its shareholders. The
14 Settlement Agreement provides APS with higher returns on equity and fair value
15 increment than is customary in the public utility industry. That alone should be reason
16 for every single customer class to demand that this rate case be fully litigated. The
17 current settlement model that has persisted for the last decade at the Commission when
18 it comes to APS means that no one ever gets the chance to actually scrutinize APS's
19 numbers. The process is flawed. And a flawed process results in a flawed outcome.

20
21 **Q. Paragraph 23.3 has a phrase stating "At APS' option...".**

- 22 • **With this statement, how can the Commission and APS customers be**
23 **assured that all customers will be treated equally and fairly by APS?**

24 **A.** Although the paragraph referenced deals with AG-X customers returning
25 to APS's alleged cost-of-service rates, the logic behind the question asked by
26 Commissioner Burns is equally applicable to everything APS does. How does anyone

1 know that APS treats one group of customers “fairly” compared to another group? Does
2 the consistent pattern of un-litigated rate cases and “comprehensive” settlement
3 agreements do anything to prevent APS from simply doing what’s best for its bottom
4 line, *i.e.*, maximizing profit for APS investors? Who can blame them when they are
5 allowed to repeat the pattern and never have to prove the details behind their proffered
6 numbers?

7 APS is granted substantial leeway in making policy decisions about how certain
8 operational costs are allocated and which customers pay for those costs. For example,
9 ED8/McMullen have made numerous data requests to APS regarding the allocation of
10 construction overhead and “loading” charges associated with APS capital expenditures
11 (“CapEx”), in hopes of discovering whether wholesale customers are treated differently
12 than retail customers. In response to those inquiries, ED8/McMullen have discovered
13 interesting information as to how APS capitalizes overhead. How a public utility treats
14 overhead becomes a very sensitive question when one remembers that the larger the rate
15 base, the larger the ultimate return for utility investors. Expenses that are incurred to
16 create plant assets are, appropriately, allowed to be capitalized as part of the cost
17 valuation of those assets. And those capitalized expenditures become a fair value
18 component of rate base on which a fair return is allowed throughout the depreciable life
19 of the assets. But virtually *every* expense item in the company—from pencils and paper
20 clips, to officers’ salaries and bonuses—could arguably be wholly or partially
21 capitalized by APS, as contributing in some way to the company’s plant.

22 The formulas and standards of practice producing these types of expense
23 allocations have a material impact upon the financial metrics of the utility. Who makes
24 those allocation policies? Who interprets the governing utility standards and makes the
25 final practice decisions for APS? Do the decisions change depending on who the CapEx
26 is for (*i.e.*, a line extension to a subdivision full of APS retail customers vs. a line

1 extension serving a wholesale District customer)? An overly aggressive practice of
2 allocating costs as capitalized expenditures could materially distort profits and equity.
3 This is especially concerning when a company like APS is spending over \$1 billion
4 annually on new CapEx.

5 **Q. Section XII deals with the costs of service study....[please explain] the**
6 **benefits and drawbacks of having the requirements of Section XII to the Settlement**
7 **Agreement for each of the below customer classes:**

8 **A.** The key phrase to remember from Section XII of the Settlement
9 Agreement is that APS agrees to make its cost of service study available to parties "**in**
10 **its next rate case**". When was the last time APS actually provided a truly transparent
11 and unbiased cost of service study—not just a model—for intervenors/Staff to review
12 prior to or *during* a rate case? The solar parties in this case have already mentioned how
13 APS's cost of service model is based on proprietary software, which doesn't allow
14 intervenors to reasonably understand the formulas that are used to reach the results
15 provided by APS. APS continues to avoid any reasonable scrutiny of its costs by the
16 Commission, because a settlement agreement is always quickly forced upon the parties
17 involved and no actual cost of service study can be thoroughly dissected and scrutinized.

18 RESPECTFULLY SUBMITTED this 18th day of April, 2017.

19 MOYES SELLERS & HENDRICKS

20 

21
22 Jason Y. Moyes
Jay I. Moyes

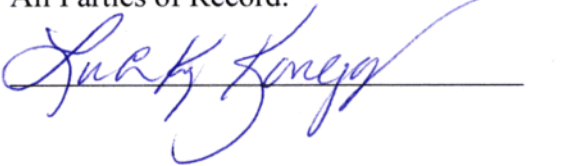
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1 ORIGINAL and 13 COPIES of
2 the foregoing filed this
3 18th day of April, 2017, with:

4 Docket Control
5 Arizona Corporation Commission
6 1200 West Washington
7 Phoenix, Arizona 85007

8 COPIES of the foregoing
9 Electronically mailed this
10 18th day of April, 2017, to:

11 All Parties of Record.

12 A handwritten signature in blue ink, appearing to read "Sarah Long", is written over a horizontal line. The signature is fluid and cursive.